Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of Deployment of Wireline Services Offering Advanced Telecommunications Capability	))))))))	CC Docket No. 98-147

COMMENTS OF THE COMMERCIAL INTERNET EXCHANGE ASSOCIATION

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COMMENTS OF THE COMMERCIAL INTERNET EXCHANGE ASSOCIATION

The Commercial Internet eXchange Association ("CIX"), by its attorneys, files these comments on the Advanced Services Notice of Proposed Rulemaking.[1] CIX is a trade association that represents over 150 Internet Service Providers who handle over 75% of the United States' Internet traffic.[2] Internet service providers, including CIX members, continue to be at the forefront of efficient, innovative and market-based Internet services to the public. Today's Internet, still widely recognized as in its infancy, is growing at an unprecedented rate and will continue to evolve into tomorrow's information superhighway. CIX believes that the NPRM is an important step towards creating a competitive market for advanced services. It sets

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1 In the Matter of Deployment of Wireline Service Offering Advanced Telecommunications Capability, Memorandum Opinion and Order, and Notice of Proposed Rulemaking, CC Dkt. Nos. 98-147, et al., FCC 98-188 (rel. Aug. 7, 1998) ("NPRM" and "MO&O").

2 The views expressed herein are those of CIX as a trade association, and are not necessarily the views of each individual member.

forth two routes for incumbent local exchange carrier ("ILEC") entry into advanced services: the integrated approach and separate affiliate approach. Under both approaches, the FCC must focus on encouraging competition in the local telecommunications markets in a manner that does not impair competition in the Internet markets.

Introduction And Summary

CIX views this proceeding as a critical juncture in the convergence of two very different industries: local telecommunications and Internet services.

Local telecommunications is defined today by monopoly providers, protective regulatory oversight of end-user services, and vertical integration and bundling of numerous local telecommunications elements and services that result in a system of complex cross-service subsidization. One of the goals of the 1996 Act is to dismantle this model of local telecommunications through the promotion of CLEC market entry. The implementation of that goal has been difficult, at best.

Internet service providers operate in a market that is diametrically opposite from today's local telecommunications monopoly. Today's Internet is based on open protocols and specialized industry offerings that collectively compose the Internet. Internet offerings are assembled from many distinct providers, including companies in: (1) end user hardware; (2) local transport; (2) Internet access; (3) application software; (4) content; and (5) backbone services. The Internet has flourished as a result of the decentralized and competitive offering of these elements, rather than through offerings that are integrated. One of the keys of the Internet success is the complete independence of one protocol layer from another. From this independence follows competition and innovation, as an industry for each protocol layer focuses on and develops responsive products. In fact, efforts to integrate these services at the cost of denying others access to the individual components have failed. As an example, the non-proprietary protocol of TCP/IP has

enabled the Internet to facilitate efficient communications by users across a variety of different interconnected networks, whereas online services based on proprietary protocols have to a large degree been unsuccessful.

This proceeding promises to bring the local telecommunications monopoly and the Internet service industries closer together, because the Commission seeks to encourage high-speed bandwidth capacity in the local telecommunications markets so that all Americans can benefit from the variety and depth of innovative Internet-based services. The proceeding is also about the Internet markets, however, because the ILECs, as long as they control the local telecommunications markets, will view unaffiliated ISPs and other Internet services as "downstream" providers to be brought under a single service package to the end-user.[3] The recent RBOC Section 706 relief petitions and the ILEC ADSL tariffs amply demonstrate that the ILECs envision a vertically integrated service: one owner of advanced data facilities and service for Americans, without regulatory protections, providing consumers a sole option from their computer all the way to, and including, the Internet backbone.

In CIX's view, the Commission should not allow this noncompetitive vertically integrated vision of advanced services, including Internet-based services, to seep into the resolution of the many technical, economic, and policy challenges presented in this proceeding. Rather, the Commission should take steps here that fortify the ability of the Internet market to operate in a competitive, decentralized, and innovative manner.

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3 See http://www.uswest.com/com/customers/interprise/ (US West states to end-users that "we've put everything together for you – complete with support – in one convenient MegaPak").

CIX believes that the objectives of a "truly" separate affiliate are commendable. A "truly" separate affiliate adds another local advanced telecommunications service provider to the market and should provide every incentive for the ILEC, and its parent holding company, to offer underlying, wholesale access services to every retail provider (CLEC or ISP). Fundamentally, CIX believes that the FCC's goal should be to separate ILEC retail incentives from wholesale incentives. This can only improve the Internet services and products that are delivered to the American consumer. However, CIX must stress that the separate subsidiary approach *only* helps consumers when there is the potential for actual and vibrant local telecommunications competition. This approach must also ensure that the ILEC's advanced services affiliate is in the same position, in every respect, as any other CLEC competitor in the market and that consumers are free to choose their ISP services.

In CIX's view, the integrated approach -- based on strict regulatory control of monopoly products and services to ensure consumer welfare -- may be a less desirable long-term solution. Cost-based and innovative local telecommunications are more likely to emerge if ILECs face competitive pressure, as called for in the 1996 Act. From the ISP perspective, the integrated approach also undermines the continuing diversity of the Internet services, especially since the current regulatory protections under the integrated model are inadequate and ineffectively enforced. However, the ILECs are likely to choose the current model of an integrated approach for voice telecommunications, advanced telecommunications, and Internet access. The Commission should, therefore, invigorate the integrated model approach with sufficient regulatory protections to, at a minimum, prevent the vertical integration of Internet services.

CIX also urges the Commission to adopt collocation and unbundling rules that improve CLECs rights under the 1996 Act to compete in the local telecommunications markets. ILEC

efforts to thwart competition through inefficient and costly collocation practices or limitations on unbundling should not be tolerated by the Commission. Further, the wholesale resale obligation should continue to apply to all ILEC advanced services.

Active and swift enforcement of the Commission's rules for advanced services competition is also necessary. CIX suggests that the Commission subject all complaints involving advanced service issues from ISPs and CLECs to its accelerated complaint process. The Commission should also develop public performance standards on a state-by-state basis of ILEC service and product provisioning to ISP and CLEC competitors.

Finally, the Commission should not adopt modifications to LATA boundaries to allow RBOC's to engage in interLATA communications to Internet NAPs. Such modifications would violate the statutory scheme and would eviscerate the Section 271 process of opening up local markets.

Discussion

I. The Commission Must Reform The Integrated Approach To Preserve Consumer Choice On The Internet.

CIX wholeheartedly agrees with the Commission that this proceeding is about ensuring competition in the marketplace for advanced services, and ensuring that all Americans reap the benefits of advanced telecommunications capability. NPRM, ¶ 84. It is critical for the Commission to reform and improve the regulatory protections that permit the ILECs to take an integrated approach toward the provision of voice telephone service, local data telecommunications service (e.g., ADSL), and Internet services.

The ILECs are likely to follow an integrated model. The RBOCs' Section 706 Petitions certainly start from the premise that monopolists can best serve the American consumer by

reaping certain "efficiencies" from vertical integration. Moreover, the public statements and comments of the ILECs indicate that the integrated model, with litigation of the MO&O, is the ILECs' general plan of implementation. The integrated model is, after all, what the ILECs have operated under for years. The regulatory contours of this model are familiar: Computer III governs regulation of information services generally, and the Non-Accounting Safeguards Order articulates the regulation of RBOC interLATA information services.

CIX questions whether the current integrated model, even if regulations are reformed, continues to serve the public interest. The integrated model under Computer III was largely based on the premise that significant internal "economies of scope" result from the integration of multiple services over common facilities.[4] Recent literature on the economics of networks has largely discredited this premise.[5] The Internet is a vivid demonstration that the asserted "economics" of vertical integration are most likely derived from monopoly leveraging, and that far more important impacts derive from the "feedback" effects of increasing returns from network externalities. These latter effects are maximized by disaggregation of a network, and not by integration.

In addition, under the integrated approach, ISPs are left with insufficient and ineffective regulatory protections. As the ILECs deploy new services, such as ADSL, through integration over the monopoly access infrastructure, these regulatory infirmities will become increasingly

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4 Third Computer Inquiry, Report and Order, 104 F.C.C.2d 958, 1008 (1986) ("Computer III") (subsequent history omitted).

5 See Milton L. Mueller, Universal Service (1997); Nicholas Economides, "The Economics of Networks," International Journal of Industrial Organization, Vol. 16, No. 4, at 673-699 (Oct., 1996).

apparent. The ILECs' aggressive entry into information services is understandable in light of the fact that the 1996 Act may actually open competition to their existing monopoly services. The ILECs are striking back by leveraging their control over the local telecommunications markets into new unregulated markets, and the Commission's rules on this entry are insufficient.

The Computer II and Computer III rules for Open Network Architecture ("ONA") access to the underlying telecommunications elements and the Comparably Efficient Interconnection ("CEI") rules promoting nondiscrimination have been largely ineffectual despite the fact that the 1994 California III remand decision called on the Commission to do more to protect ISPs.[6] When reformed, the rules of ISP access and nondiscrimination are likely to be the underpinnings of ISP protections under the integrated approach. If these rules are unsettled, further delayed, or easily avoided, then the integrated approach leaves the Internet market at significant risk of ILEC vertical integration and discrimination. CIX urges the Commission to revamp and strengthen the regulatory protections under the integrated approach.

The problem is real: the Internet industry is today adversely affected by the lack of adequate safeguards under the Computer III-type regulations. The ONA process – designed to provide efficient access to underlying telecommunications services – is today an elaborate federal process that has not measured up to the Commission's plan. This is not because unbundled elements would not be demanded by ISPs. Rather, the process yields too much

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6 In California III, the court vacated the Commission's Computer III Safeguards Order because it found that the FCC had set out "fundamental unbundling as a key safeguard against access discrimination," and yet the "apparent retreat" from enforcement obligations of ONA had "failed to prevent the BOCs from engaging in discrimination against competing ESPs in providing access to basic services." California v. FCC, 39 F.2d 919, 929 (9th Cir.), cert. denied, 115 S. Ct. 1427 (1994) ("California III").

discretion and control to the RBOCs. Under the integrated approach, the monopolist cannot control its own unbundling/access implementation.

Further, under Computer III, the ILEC affiliated ISP is permitted to physically collocate in ILEC central offices, while such collocation is denied to all other independent ISPs.[7] While the Commission's Computer III decision may have had justification at the time, it is today resulting in a technical and market monopoly advantage for the ILEC-affiliated ISP that is deeply antithetical to the principles of nondiscrimination in the ISP market. This sort of monopoly discrimination would not be permitted in the telecommunications markets, and the Commission should not allow ILECs to discriminate in the ISP market.

Moreover, the provisioning of ILEC services to independent ISPs is notoriously slow and inadequate, despite the Computer III proscription against such conduct. CIX suggests that the Commission establish public data collection and performance standards for the ILEC provisioning of services to ISPs, and to its own affiliated-ISP, for such services as business lines, T1 lines, T3 lines, and ISDN lines.

In addition, the ILECs are regularly promoting bundled service plans combining local telephone, data telecommunications (e.g., DSL), hardware, installation, and Internet.[8] Despite the Computer II "all carrier" rule to tariff the underlying telecommunications services separately from the information services, the ILECs have undercut the intent of that rule by mass marketing bundled service in a way that precludes consumers from making rational economic decisions to

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[7] Computer III, 104 F.C.C. 2d at 1038.

take one component, such as ILEC DSL, and to access another ISP's services.[9] This bundling is fundamentally contrary to the goals of an openly competitive ISP marketplace. It also suggests significant cross subsidization from the regulated services to the unregulated ISP services. Cf., 47 U.S.C. § 254(k) ("A telecommunications carrier may not use services that are not competitive to subsidize services that are subject to competition.").

The integrated approach also provides consumers with no right to select their ISP of choice.[10] CIX believes there should be an affirmative "ISP Choice" obligation so that consumers can select among several ISPs serving the market. Commission action to preserve ISPs should take two directions. First, consumers should be able to select the ISP they want regardless of the ILEC's underlying telecommunications decisions, and the ILEC should not be allowed to skew the end-user's decision by advantaging its ISP affiliate in the ISP market. Second, to ensure that

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8 BellSouth's FastAccess service provides ADSL service and Internet access at $49.95 for its voice customers, and at $59.95 for ADSL and Internet access on a "stand alone" basis. See http://www.bellsouth.net/external/adsl/cost.html.

9 Bell Atlantic, for example, puts considerable economic pressure against choosing an independent ISP. See www.bell-atl.com/adsl/more_info/pricing.html. Bell Atlantic offers a 12 month package of bundled Bell Atlantic ISP, DSL, ethernet card, service connection charge, and DSL modem for as rates as low as $59.95/mo and $99 for the DSL modem. However, if the customer chooses another ISP, the customer may be charged: service connection charge -- $99.00; DSL modem -- $325.00 (or 162.50 for residential users); turnkey home installation -- $99.00; cost of ethernet card (approximately $100.00).

10 In an analog environment, customers had a rudimentary form of ISP choice by dialing the ISP's telephone number. With "always on" DSL, however, customers lose that functionality.

consumers have viable choices among ISPs, the market for transport services to the competing ISPs should be open to competition.

The Commission has also established insufficient safeguards for RBOC entry into the interLATA Internet service markets. Specifically, the Non-Accounting Safeguards Order[11] offers the RBOCs far too much ambiguity in the terms "teaming," as well as resale, "bundling," and the ways in which RBOCs can connect to interLATA Internet providers.[12] This ambiguity has led to RBOC arrangements with global service providers that raise questions of interLATA Internet activities prior to Section 271 approval. CIX and other parties have raised these issues in the SouthWestern Bell Company CEI Plan proceeding.[13] Despite these significant questions of statutory compliance, the Commission has yet to address these matters.

CIX asks the Commission to undertake in this proceeding a thorough review of the regulatory safeguards under the integrated approach. The Commission should better ensure that ILECs (a) provide efficient and nondiscriminatory underlying telecommunication inputs to ISPs, (b) offer access to facilities, including collocation, on terms that are equal for all ISPs, (c) engage in bundling/marketing practices for regulated and nonregulated services only if consumers are

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11 Non-Accounting Safeguards of Sections 271 and 272 of the Communications Act, First Report and Order, 11 FCC Rcd. 21905, ¶ 289 (1996) ("Non-Accounting Safeguards Order").

12 Id. at ¶ 119.

13 Southwestern Bell Telephone Company's Comparably Efficient Interconnection Plan for the Provision of Internet Support Services, CCB Pol 9705, 12 FCC Rcd. 6853 (1997). In that case, Southwestern Bell ("SWB") proposed to align with a single GSP and to bundle both services together. Evidence of bundling included (1) all SWB customers must subscribe to the designated GSP service, (2) SWB will act as agent for the GSP at the same time as the customer signs up for SBW Internet service, and (3)

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provided with a viable opportunity to choose among ISPs, and (d) do not cross-subsidize ISP service with other revenues derived from regulated services. Further, CIX suggests that the Commission should prevent the vertical integration of the ISP market by providing ISPs with a method of bypass -- functional and cost-based ISP access to ONA-type services, including unbundled local loops. Finally, the Commission should investigate whether (a) there is continuing efficacy under the vertically integrated model, and (b) the marketing/bundling practices of the ILECs' regulated telecommunications services with its ISP service and with the interLATA global service provider services are consistent with law and serve the public interest.

In sum, CIX believes that if the integrated approach is designed to rely on monopoly regulation for the protection of the "downstream" independent providers of Internet services and the prevention of ILEC vertical integration, then those regulations must be brought up to the task and enforcement must be vigilant.

II. Advanced Services Separate Affiliates Of The ILEC Must Not Obtain Any Competitive Advantage Through Its Affiliation With The ILEC Or Its Parent Holding Company.

In CIX's view, the separate subsidiary approach undertakes to protect consumers by promoting competition between firms that have no monopoly advantages of any kind in the underlying local telecommunications. In that way, advance service firms are motivated to serve retail customers, and not other interests. Under this model, the ILEC serves all retail providers

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SWB is compensated through a per-customer commission, which ties SWB to the success or failure of the GSP's offering.

indifferently with local loops, collocation, and other telecommunications inputs, and is indifferent as to which retail providers succeed or fail.

The Commission's role under a separate subsidiary model should be to ensure that the affiliate derives no advantage as a result of its affiliation with the incumbent LEC. CIX believes that separate affiliates must be operationally, managerially, financially, and technically separate from the ILEC. The Commission should establish a procedure to "certify" that an ILEC affiliate, in fact, complies with its requirements before that affiliate is permitted to operate. Mere ILEC statements or assertions of compliance with the separate affiliate rules are insufficient. The BOCs' record of facial BOC noncompliance with Section 272 -- despite their assertions that they have met the requirements of that section – indicates that the Commission cannot rely on ILEC assurances that they will follow its rules.

The affiliate separation should be designed to remove the ability of the ILEC and its parent holding company --with their tremendous monopoly advantages -- to favor the retail offerings of both the advanced services affiliate and the affiliated ISP. No ILECs should be "waived out" of the obligations to comply. Smaller ILECs are just as capable of discriminating in favor of their affiliates and other abuses as are the RBOCs.[14] Further, CIX believes that consideration of "sunset provisions" of the separate subsidiary rules is premature.[15] Once the rules are in place and the quickly-moving market stabilizes, then the Commission and industry can better assess "sunset" issues.

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14 NPRM, ¶ 98.

15 Id., ¶ 99.

A. Rigorous Structural Separation and Non-Discrimination Requirements Should Be Placed on ILEC Affiliates.

At ¶ 96 of the NPRM, the Commission proposes structural separation and nondiscrimination requirements for the advanced services separate affiliate. These requirements are grounded in the 1996 Act,[16] and are necessary, but not sufficient, to ensure that independent providers are protected from discrimination.

The most fundamental of these safeguards is that the incumbent must "operate independently" from its affiliate in all ways, including separate ownership of switching facilities and property on which these facilities are located, as well as the maintenance of separate books, records, and accounts. Without independent operations, the separate affiliate will be little more than a retail arm of the incumbent and the ILEC has merely avoided its obligations through corporate "shells." For this same reason, all transactions between the ILEC and its affiliate must be at "arm's length" and available for public inspection. The transparency of these transactions will reduce the temptation of the ILEC affiliate to gain advantages over competitors by sharing costs and resources.

These safeguards must also address that the current ADSL offerings of the ILECs bundle the underlying telecommunications service with Internet access and offer these combined services as a single retail package.[17] While the Section 272 safeguards should provide ISPs with full rights to the "goods, services, facilities, and information" provided by the ILEC to its

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16 47 U.S.C. § 272 (b), (c).

17 See, e.g., <http://www.ameritech.com/products/data/adsl/index.html> (Ameritech describes its Internet service as ADSL service).

affiliate,[18] the NPRM does not sufficiently explore how the bundled ADSL offerings impact competing ISPs. As the ILECs separate affiliate will likely offer its ADSL service in a manner similar to the current ILEC bundled offerings, independent safeguards must also exist to protect the competitive ISP market. Without such safeguards the bundled offering of the affiliate may foreclose the independent ISPs from offering Internet access over ADSL services on competitive terms.

For example, as the ADSL offering of the affiliate will be billed at a single price and included on the same bill, the advanced services affiliate will have reduced billing, mailing and collection costs. Independent ISPs, however, will have to incur the costs of separate billing and collections. CIX believes this is plainly inconsistent with Section 272 safeguards for "goods, services, and facilities" to be provided to an affiliated ISP or CLEC, while those same services are unavailable to independent providers.

B. Additional Structural and Nondiscrimination Safeguards Are Also Necessary Because ILECs Have Not Yet Opened Local Markets.

In addition to the protections enumerated in the NPRM, the Commission should adopt stronger safeguards to further limit the ability of the ILECs to discriminate against competing providers. These additional safeguards are necessary because of the ILECs' continuing monopoly. The Section 272 separate affiliate safeguards assume that the ILEC has fulfilled its Section 271 obligations. In this case, however, the Section 271 "competitive checklist" will not have been met and so additional safeguards above and beyond those established in section 272 must be established for the proposed advanced services affiliates.

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[18] Non-Accounting Safeguards Order, ¶ 219.

1. Marketing Practices: the ILEC Name & CPNI, Joint Marketing, Resale, and the "Price Squeeze"

The existing relationship built between the ILEC and its customer is a considerable vestige of the ILECs' decades-long role as monopoly provider to all customers in the market. This market presence, if transferred to the advanced services affiliate, represents an "intangible" asset or "good will" that is of considerable value vis-à-vis other competing providers of advanced services. The Commission should prevent the affiliate and affiliated-ISP from leveraging this "good will" value by using the ILEC's name. Whether one considers this value a "de minimis" transfer issue or an attribute of the monopoly, the ILECs' affiliates competing in deregulated markets – the affiliated CLEC and ISP – should not be able to usurp this advantage.

Another example of this potential marketing advantage is use of the ILEC's CPNI. CPNI is a critical marketing tool for targeting potential customers, and maximizing return on sales, advertising, and business development expenses. For independent advance service providers (CLECs or ISPs), however, there is significant cost associated with obtaining the same market information. In CIX's view, the affiliate should not be permitted to take advantage of the ILEC's CPNI in this way. Thus, the ILEC's CPNI should be available equally to all CLEC and ISP competitors, or the ILEC should be barred from sharing CPNI with its advanced service and ISP affiliates.

Joint marketing efforts between the ILEC and the affiliate also pose significant risk that the transaction is not at "arms length." Both the Commission and the Congress have recognized

the unique competitive advantages that result from joint marketing with the ILEC.[19] Through joint marketing, the ILEC may absorb the affiliate's share of the marketing costs and thereby reduce or eliminate this normal business expense for the affiliate. There is also an inherent advantage of joint marketing that stems from the appearance of a service offered by the ILEC, which holds vestiges of the quasi "public utility" in its role as monopoly provider. To avoid this advantage and customer confusion, safeguards should be adopted prohibiting such joint marketing of advanced services with the ILEC's voice service.[20]

An anti-competitive marketing advantage also arises if the advanced service affiliate is able to sell a single, bundled local telephony/data/ISP package. For example, the ILEC affiliate could "add" ADSL service to the voice service of the ILEC using the same customer loop. To avoid discriminatory resale, the Commission should ensure that the voice services are available for resale by unaffiliated CLECs, and that all competing providers may purchase the voice service at the same price. This safeguard is consistent with Section 272(g)(1) and the Non-Accounting Safeguards Order.[21]

Moreover, if competitors do not have equal ability to resell the voice service of the ILEC, then the affiliate engaged in resale of voice service is, for all practical purposes, a "successor or

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19 47 U.S.C. § 271(e); Non-Accounting Safeguards Order, ¶¶ 277-281.

20 Such a restriction would be consistent with the Non-Accounting Safeguards Order (at ¶ 280) that a "carrier may not mislead the public by stating or implying that it may offer bundled packages of interLATA service and BOC resold service, or that it can provide 'one-stop shopping' of both services through a single transaction.".

21 "A Section 272 affiliate may not market or sell information services and BOC telephone exchange services unless the BOC permits other information service

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assign" or "comparable carrier" under Section 251(h). Section 251(h) treats any local exchange carrier as an ILEC if that carrier occupies a market position comparable to that of an ILEC, the carrier has substantially replaced the ILEC, and the treatment is consistent with the public interest. 47 U.S.C. § 251(h)(2). Without equal resale rights for competitors, the affiliate stands in the same monopolist position as the ILEC. The ability to resell ILEC voice service with advanced services prior to full compliance with the local competition provisions of the 1996 Act would also disincent the ILEC from complying with its statutory obligations. The formation of an advanced services affiliate should in no way reduce the incentives created in the 1996 Act to encourage the opening of local markets to competition.

Finally, adequate safeguards need to address the possibility of a "price squeeze." A price squeeze could occur either in the data CLEC market (by imposing high UNE pricing for competitors and offering low-priced retail DSL-affiliate services) or the ISP market (by offering high transport and other telecommunications to all ISPs and offering low-priced retail ISP-affiliate services). The Commission should establish rules, and a process of price review, designed to eliminate the ability of the ILEC and its affiliates to engage in a "price squeeze."

2. Parent-Holding Company Relationship to Affiliate, and Affiliate Ownership Issues.

In any regulated separate subsidiary model, the parent holding company and the ILEC have the same incentive for anti-competitive conduct. Therefore, the parent holding company should not be allowed to accomplish indirectly what the ILEC is prohibited from doing directly.

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providers to market and sell telephone exchange services." Non-Accounting Safeguards Order, ¶ 287.

Monopoly profits passed from the ILEC onto the parent company (or another affiliate) keep the profits in the "family." However, if these profits can then seep into either the CLEC or ISP affiliate through the parent company, the ILEC monopoly and its monopoly rents are, in essence, funding the affiliate. This indirect funding would allow the affiliate to undercut competitors by offering services at prices below competitive levels in order to capture customers for the purpose of vertical integration.

CIX believes it is appropriate for the Commission to establish affiliate-transaction rules that foreclose the ability of the ILEC, directly or indirectly, to offer favorable financial terms to its CLEC or ISP affiliate. Under the separate subsidiary model, the affiliate should face the same competitive market for initial capitalization and subsequent financing as any other competitor. The burden of proof should be on the affiliate to demonstrate that the terms of financing (e.g., interest rate, term, default terms) are generally consistent with other competitors in the market, if the affiliate chooses to use the financial resources of its ILEC or parent. This restriction would preserve the underlying purpose of the safeguards to ensure that the affiliate deal at "arms-length" with the ILEC, and should ensure that the affiliate is not able to benefit in the extension of credit, funds, profits, or personnel through opportunities that are unavailable to competitors.

Finally, the Commission should require that some truly independent, non-affiliated investor(s) hold a minority ownership share (e.g., 10% or 20%) in the affiliate. With minority owners, the corporate relationships and transactions between affiliates would be subject to considerably more discipline due to the fiduciary duties owed to outside shareholders. Some independent ownership would also reduce the likelihood of a "price squeeze" because the affiliate would be much less inclined to act in a concerted manner with the ILEC. Fundamentally, separation of ownership tends to encourage the ILEC to become a wholesale

provider of local telecommunications, as the affiliate focuses on competing in the advanced services retail market.

3. Access/Interconnection with Affiliate's Facilities

The offering of services using different technologies than the traditional circuit switched PSTN through an unregulated separate affiliate should not result in the extension of the ILEC monopoly. However, if the ILEC affiliate can penetrate the market with new services (e.g., ADSL) before independent competitors have had the opportunity to penetrate those markets, or to adequately adjust to regulatory changes, the introduction of the Commission's advanced services regulations could disrupt CLEC competition. For example, CLECs relying on the Commission's MO&O may adopt a resale-based approach. However, such CLECs (and their customers) could be abruptly dislocated should the Commission adopt its separate subsidiary proposal and the ILEC decide to take that approach.

In order to ensure that competitors' can adjust to regulatory changes or the next ILEC service roll-out, CLECs should be provided with cost-based resale access to the advanced services affiliate's DSLAM and other facilities required to provide advanced services, on an interim basis. CIX recommends that the Commission establish a transition period for such resale that will enable CLECs to move from complete resale to facilities-based offerings. This transitional resale rule recognizes that, while an advanced service affiliate should be lifted from Section 251(c) obligations, it is also true that CLEC competition and DSLAM deployment will take time. American consumers should not, however, have to wait additional years for competitive data offerings. The need for such a transition is heightened where the underlying advanced services network elements were, in fact, ILEC property merely transferred from the ILEC to the affiliate under a *de minimis* exception.

The transition period for resale of advanced services facilities should expire either when the ILEC has met its Section 271 checklist or in two years. If sufficient competitive requirements have been met by the incumbent, then this safeguard will no longer be necessary. Alternatively, two years should provide competitors and new entrants with sufficient time to deploy advanced services in a manner that enables them to compete with the affiliate.

In addition, as the advanced services affiliate and other data CLECs deploy their networks, interconnection between the different advanced local networks is of critical importance to both CLECs and ISPs. The Commission has recognized that functional interconnection protects ISP competition from ILEC discrimination, and opens the ILEC local network for alternative ISP usage.[22] Interconnection is also important when advanced services are offered through the separate affiliate, which is subject to the interconnection obligations of Sections 251(a) and (b) of the Act. Without such interconnection, independent ISPs will be forced to establish separate trunk connections to the network of each data CLEC in a given region. As a practical matter, this puts independent ISPs at an insurmountable competitive disadvantage vis-à-vis the affiliated ISPs. In addition, a lack of interconnected data networks in a given market increases ISP transport costs. By contrast, interconnection of the ILEC affiliate's network with other local data network providers (including CLECs) encourages a market for

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22 See, e.g., Computer III Remand Proceedings, Report and Order, 5 FCC Rcd. 7719, 7720 (1990); MO&O at ¶ 37 ("BOCs offering information services to end users of their advanced service offerings, such as xDSL, are under a continuing obligation to offer competing ISPs nondiscriminatory access to the telecommunications services utilized by the BOC information services."); id. at ¶ 48 (" . . . interconnection obligations of sections 251(a) and 251(c)(2) apply to incumbent's packet-switched telecommunications networks and the telecommunications services offered over them.").

competitive transport services to ISPs, such as Data Competitive Access Provider ("DCAP") service.

ISP offerings and consumer prices are directly impacted by the cost and efficiencies associated with these transport arrangements. For this reason, the Commission should encourage the offering of DCAP service, which aggregates ISP traffic in competition with the ILEC's metropolitan area transport services. The resulting competition in the DCAP market will, in turn, allow ISPs to reach all customers in a given market, decrease the cost of ISP service, and encourage ISPs to roll-out innovative offerings.

4. Advanced Service Affiliate's Treatment of Independent ISPs

The Commission must regulate the advanced telecommunications services in a manner that promotes ISP competition in the market and ISP choice for end users. In Computer II, and subsequently reinforced in the AT&T Frame Relay Order, the "all carrier" rule that requires the affiliate "that own[s] common carrier transmission facilities and provide[s] enhanced services, but are not subject to the separate subsidiary requirement, must acquire transmission capacity pursuant to the same prices, terms, and conditions reflected in their tariffs when their own facilities are utilized."[23] ISPs should continue to have equal pricing, terms, and conditions to underlying telecommunications as the ILEC affiliated ISP. The Commission should clarify that these existing obligations apply fully to the affiliate CLEC, so that all ISPs are able to purchase underlying telecommunications and interconnection arrangements that are offered to the affiliated ISPs.

Adherence to the "all carrier" rule will also further the concept of ISP choice. ISP choice is the ability of a customer to select any ISP offering service within the market.[24] This ability is contingent upon (a) the independent ISP being able to offer its service on equal terms in relation to the ILEC advanced services affiliate, and (b) the ILEC or its affiliate not forcing or steering customers to the ILEC affiliated ISP in its marketing or initial contacts with the customer. In practice, a customer ordering an advanced services affiliate's ADSL offering should be given their choice of ISP, at no additional costs for selecting an independent ISP.

C. ILEC Transfers To Affiliates

As both a matter of law and policy, it is important to restrict transfers from the ILEC to the separate affiliate. Section 251(h) of the 1996 Act appears to limit any sale or conveyance by the ILEC of facilities or network elements (existing and future) to the advanced services affiliate; such transfers may eliminate the separate affiliate status, subjecting the affiliate to ILEC regulatory obligations. The policy rationale underlying this statutory provision is plain: the affiliate must be truly "separate," and it may not step into the place of its ILEC affiliate.

To preserve this important policy objective, CIX believes that any *de minimis* exception for the transfer of facilities should be very limited. The types of facilities permitted to be transferred under this exception should be limited exclusively to DSLAMs and packet switches.

(footnote continued from previous page)

23 AT&T Frame Relay Declaratory Ruling, Memorandum Opinion and Order, 10 FCC Rcd 13717, 13725 (1995).

24 See also CIX Comments on Notice of Inquiry, CC Dkt. No. 98-146, at 17-20 (filed Sept. 14, 1998).

No other transfers (such as real estate, employees, customer accounts, or brand names) should be permitted. The affiliate should be required to pay for the transferable facilities at no less than fair market value; the ILEC cannot simply "give away" the equipment. Such facilities should be fully subject to the nondiscrimination requirement of Section 272(c)(1), and the terms of transfer should be equally available to all competitors (such as through an auction). Further, with any such transfer, the burden should be on the ILEC to demonstrate that the equipment was transferred at fair market value. Where the property is sold at auction, the ILEC should provide an independent estimate that the value of the property was not less than the auction price. Finally, to avoid the expense of continuing regulatory oversight of transfers, the exception should apply only to facilities acquired prior to the release of the NPRM, and no such transfers should be permitted six months or more after the release of the Order in this proceeding.

CIX agrees with the tentative conclusion of the NPRM (at ¶ 110) that, to the extent there are any space limitations on the incumbent LEC's premises (either at the central office or remote terminal), the affiliate should not be permitted to leave such transferred equipment in its current location. In this way, competitors are not "closed out" of central offices and the affiliate does not reap a "collocation premium" that is not reflected in the transfer price of the equipment. Some ILECs may have already widely deployed DSL facilities. For example, US West is already offering its "Megabit" ADSL services in a total of over 150 central offices in all 14 of its states.[25] With such significant deployment, a safeguard preventing transfer of a "collocation premium" is a sensible way to ensure that the affiliate does not unfairly benefit from the ILEC's prior monopoly-based deployment.